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# IN THE SUPREME COURT OF THE UNITED STATES

## OCTOBER TERM, 1954

NO. [redacted]106

STAPLING MACHINES CO. ..... Appellant

Vs.

A. H. STONE, CHAIRMAN
STATE TAX COMMISSION ..... Appellee

## BRIEF OF APPELLANT IN REPLY TO STATEMENT OF APPELLEE OPPOSING JURISDICTION AND MOTION TO DISMISS OR AFFIRM

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May it please the Court:

## BRIEF IN SUPPORT OF PETITION FOR APPEAL

### I.

### STATEMENT OF FACTS AND ISSUES ON APPEAL

Appellant, Stapling Machines Co., is a Delaware corporation domiciled in Rockaway, New Jersey, and is the owner of patents covering box-making machines and patented boxes and is engaged solely in the *licensing* of patent rights to licensees in the State of Mississippi. The company *is not* engaged in Mississippi in the *renting or leasing* of personal property and is engaged only in licensing the patents which it owns, all of which are located in the State of New Jersey.

The record on appeal will disclose that a license agreement was entered into between the licensor, Stapling Machines Co., Appellant in this case, and various licensees in Mississippi. The license agreements were all entered into in the State of New Jersey, whereby the licensees agreed to pay to the licensor a royalty for the use of the patented machines amounting to two percent of the gross sales or fair market value, whichever was higher, and an additional two percent for the use of its patents to manufacture patented boxes. There is no provision in the license agreement for the payment of rent, as such. As a corollary to this agreement, the licensee is required and does pay to the licensor one hundred and five percent of the value of the machine which is delivered to the licensee in the State of New Jersey and moved to the State of Mississippi under the direction and designation of the licensee, and the location of the machines is only for the convenience of the licensee. From that time forward, Stapling Machines Co., Appellant, has no control whatsoever over the machines except for the purpose of inspecting and sketching for study in connection with future patent improvements.

Title is retained in the machines by this licensor solely for the purpose of protecting its patent rights, as the company has been fully reimbursed for the expense of manufacture of the machines. The Stapling Machines Co., Appellant, is not present in Mississippi for any purpose. They have no offices, agents or employees of any kind in this State at any time, and they have not qualified to do business in Mississippi. The license agreements are entered into in the State of New Jersey.

The pleadings in the record will show that under the license agreement all ad valorem taxes are paid by the licensee on the machines for protection by the State of

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Mississippi, and the record will further show that all taxes required by New Jersey, the State of domicile, are paid by the Appellant to that State. The Appellee in this case, the State Tax Commission, attempts to impose a privilege and license tax on this activity which they have admitted is wholly and completely in interstate commerce, and which does not have a business situs in Mississippi. Excerpts from the statute imposing the tax, which statute is shown in complete detail in Appendix "3" to the Appeal, are as follows:

CHAPTER 119, LAWS OF 1934 AS AMENDED BY MISSISSIPPI CODE OF 1942 (RECOMPILED), CHAPTER 3.

Section 10,105. Tax levied. — There is hereby levied and shall be collected annual privilege taxes, measured by the amount or volume of business done, against the persons, on account of the business activities, and in the amounts to be determined by the application of rates against values, or gross income, or gross proceeds of sales, as the case may be, as follows:

Section 10,111. Miscellaneous business. — (1) Upon every person engaging or continuing within this state in any of the following businesses, there is likewise hereby levied and shall be collected a tax on account of the business engaged in equal to two per cent of the gross income of the business:

* * * Renting or leasing of tangible personal property. * * *

Section 10,115. Permit to engage in business. — Any person who engages, or who intends to engage, in any business or activity which will subject such person to a privilege tax imposed by this act, shall apply to the commissioner for a permit to engage in and to conduct

any business or activity upon the condition that he shall pay the tax accruing to the State of Mississippi under the provisions of this act; and shall keep adequate records of such business or activity as required by section 8 (Sec. 10120) of this act. Upon receipt of such permit, the applicant shall be duly licensed under this act to engage in and conduct such business or activity. Said permit shall continue in force so long as the person to whom it is issued shall continue in the same business at the same location, unless revoked by the commissioner for cause.

The Commissioner is hereby authorized to revoke the permit of any person failing to comply with any of the provisions of this act, after giving to the person holding such permit ten (10) days' notice of the intention of the commissioner to revoke such license. Unless good cause be shown within said ten (10) days why such permit should not be revoked, the commissioner may revoke such permit, and revocation of such permit, or engaging or continuing in business after such permit is revoked, shall subject such person to all the penalties imposed by section 16 (10133) of this act.

Any person liable for a tax under the provisions of this act who fails to obtain a permit from the commissioner or who continues in business after such permit has been revoked, or who fails to make his returns for taxation as provided in section 6 (10118) of this act, or who fails to keep adequate records and invoices provided by section 8 (10120) of this act, or who fails or refuses to permit inspection of such records, or who fails to pay any taxes due hereunder, shall forfeit his rights to do business in this state until he complies with all the provisions of this act and until he enters

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into a bond, with sureties, to be approved by the commissioner, in an amount not to exceed twice the amount of all taxes estimated to become due under this act by said person for any three (3) month period, conditioned to comply with the provisions of this act, and pay all taxes legally due by him.

The commissioner shall require of every person desiring to engage in business within this state, who maintains no permanent place of business within the state, a cash bond or an approved surety bond in an amount sufficient to cover twice the estimated tax liability for a period of three (3) months. Provided, however, that the bond shall in no case be less than one hundred dollars ($100.00) and that the tax may be prepaid in lieu of filing bond if the amount is approved by the commissioner. This bond shall be filed with the commissioner prior to the issuance of a permit to do business and before any such person may engage in business within this state. Failure to comply with this provision will subject such person to the penalties provided by section 16 (10133) of this act.

If any person is engaged in or continuing in this state in any business or activity without obtaining a permit, or after such permit has been revoked, or without filing a required bond, or without keeping and allowing inspection of all records required by this act, or without making a return, or returns, and without paying all taxes due by him hereunder, it shall be the duty of the commissioner, or the attorney general when requested by the commissioner, to proceed by injunction to prevent the continuance of said business. Any temporary injunction enjoining the continuance of such business shall be granted without notice by a judge or chancellor now authorized to grant injunctions.

The Tax Commission, in attempting to apply this tax did so in an arbitrary manner, and it was so held by the Court of original jurisdiction.

## STATEMENT AT TO JURISDICTION

Appellant submits herewith its statement particularly disclosing the basis upon which the Supreme Court has jurisdiction on appeal to review the Judgment of the Supreme Court of the State of Mississippi entered in this cause.

### Opinion Below

The opinion of the Supreme Court of the State of Mississippi, which is the highest Court of this State, indicates that said Court has decided a Federal question of substance in a way not in accord with applicable decisions of this Court. S. Ct. Rule 38,5(a). The Supreme Court of Mississippi has decided that an undomesticated foreign corporation engaged in business exclusively in interstate commerce must pay Mississippi a tax for the privilege of engaging in such commerce, even though it does not have a business situs in Mississippi.

### Jurisdiction

The Judgment of the Supreme Court of the State of Mississippi was entered on March 22, 1954, the plaintiff-appellant's suggestion of error was overruled April 19, 1954, a petition for appeal to the Supreme Court of the United States presented to the presiding Justice of the Supreme Court of the State of Mississippi, on the 11th day of May, 1954. The jurisdiction of the Supreme Court of the United States to review this decision by direct appeal is confirmed by Title 28, United States Code, Section 1257(a).

The following decisions sustain jurisdiction of the Supreme Court of the United States to review the judgment on direct appeal in this case:

*Nippert v. City of Richmond*, 327 US 416, 90 L ed 760

*Davis v. Virginia* 236 US 697, 59 L ed 795

*Caldwell v. State of North Carolina* 187 US 622, 47 L ed 336

*Dozier v. State of Alabama* 218 US 124, 54 L ed 965

*Craig v. Mills* 33 So. (2d) 801, 203 Miss 692

*Crutcher v. Kentucky* (1891) 141 US 47, 35 L ed 649

*Webber v. Virginia* (1880) 103 US 344, 26 L ed 565

*Robbins v. Tax District of Shelby County, (Tenn)* 120 US 489 30 L ed 964

*William G. Asher v. State of Texas* 128 US 129, 32 L ed 368

*International Textbook Co. v. Pigg*, 217 US 91, 54 L ed 678

*Memphis Steam Laundry Cleaners, Inc. v. A. H. Stone, Chairman State Tax Commission* S. Ct. 96 L ed 436

## The Precise Questions Involved

The questions involved in this case and presented to the Court for its decision are as to whether or not Chapter 119, Laws of 1934, as amended, Mississippi Code of 1942, (Recompiled) Chapter 3, Sections 10,105, 10,111, 10,115, 10,120 and 10,123 violate Paragraph 3, Section 8, of the Constitution of the United States providing that Congress shall have power to regulate commerce with foreign nations and among the several states and with the Indian Tribes, and as to whether or not such paragraphs violate Section (1) of the 14th Amendment to the Constitution of the United States providing that no state shall

deprive any persons of life, liberty and property without due process of law nor deny to any person within its jurisdiction the equal protection of the law.

The Supreme Court of Mississippi held that the sections were valid and did not violate either the commerce clause or the 14th Amendment to the Constitution of the United States. The Federal question in this cause was properly, timely and fully raised by Stapling Machines Co. and squarely passed upon by the Mississippi Supreme Court.

## II

## A SUBSTANTIAL FEDERAL QUESTION IS INVOLVED IN THIS CAUSE

The facts in the case appear from the pleadings and testimony and are undisputed. (R 2). The appellant's declaration alleged that it was a foreign corporation organized under the laws of the State of Delaware but whose domicile and principal place of business and all offices and officers are located in Rockaway, New Jersey, and that it was engaged in licensing patented machines and patents covering different types of boxes made by said machine, and which patents are made the subject of license agreements with licensees in the State of Mississippi. That it has no offices, officers, agents, employees, representatives, and no place of business located in the State of Mississippi. All of its transactions are in interstate commerce, and all of the patents are located in New Jersey, and, therefore, not subject to a privilege tax by the State. That all license agreements are entered into in the State of New Jersey, where patented machines are delivered to the licensee f.o.b. Rockaway, New Jersey, after having been paid the sum of one hundred and five percent of the cost.

The State Tax Commission has attempted to impose a privilege tax as a condition precedent to entering into the license agreements with licensees in the State of Mississippi, and has cited the Stapling Machines Co. to appear and show cause why it should not be required to pay the privilege taxes imposed by Chapter 119, Laws of 1934, as amended, Mississippi Code of 1942, (Recompiled) Chapter 3, Sections 10,105, 10,111, 10,115, 10,120, and 10,123. (R 8)

The tax is 2 percent of the gross dollars received from the aforesaid license agreements.

Appellant filed with the State Tax Commission a comprehensive statement of the nature and scope of its business in Mississippi and alleged that the imposition of the tax violates constitutional immunities in that the State had no jurisdiction to tax the income from the intangible patent rights, as they had no business situs within the state and also the state's statutory definition of "doing business" could not confer such jurisdiction; that its activities were wholly and completely in interstate commerce and therefore not subject to privilege taxation by the state. The Commission disagreed with Appellant and entered an order sustaining the tax liability. (R 9).

Appellant appealed to the Circuit Court of the First Judicial District of Hinds County, Mississippi, raising these questions by its pleadings. (R 6). The Circuit Court reversed the Tax Commission and held Appellant not liable for the taxes, on the ground, as stated in the opinion, that:

> "From the pleadings and the admission contained therein it appears to me that the entire transaction is in Interstate Commerce. • • • This defense of the transaction, being violative of Commerce Clause of the

United States Constitution, is a total defense, and if good, would, of course, bar the tax and warrant the recovery." (R 69-70)

The Supreme Court of Mississippi reversed the Circuit Court and entered a final judgment dismissing Appellant's suit and the amount sued for for the years 1949 and 1950.

The Supreme Court of Mississippi summarized in its opinion the undisputed facts, as follows:

"The appellant contends that the tax here collected was two per cent of the gross income of appellee from its business of renting or leasing tangible personal property in the state. On the contrary, the appellee contends that the income in question did not arise from rents, but was royalty, and, as such, was not taxable. The decision of this controversy also involves a consideration of what constitutes doing business, the situs of property for taxation, and the commerce clause of the federal constitution.

"The appellee is a Delaware corporation, having a place of business in Rockaway, New Jersey. It leased, under a written contract, to certain persons in the State of Mississippi, delivered f.o.b. the place of manufacture, at the cost of production, certain box making machines on which it held U. S. patents. The lessees thereunder acquired no property rights other than the right to use. The company agreed to furnish repair parts. Its agents were granted access to the machines for inspection and sketching. It had no office or agent in the state. The obligations of the lessees were payable at its principal place of business; and the lessees were required to keep accurate records, separate and apart, and subject to examination by the company's agents

who had the right to make copies. The lessees were also required to report in writing to the company the number of boxes delivered during the past month, to whom sold, and the gross amount thereof.

"Under Section 1 of the lease contract, the lessee had 'the right and license (a) to make on Lessor's machines in the factory of Lessee at Jackson, Mississippi, boxes covered by any one or more of the patents listed in Exhibit A; (b) to use in said factory, for the manufacture of boxes, machines leased hereunder from Lessor; (c) to use in said factory, for the manufacture of boxes on Lessor's machines, the method inventions covered by any one or more of said patents; and (d) to sell in the United States boxes made under this agreement.

"Thus it will be seen that the lessees had the right to use the patented machines, to make patented boxes thereon, to use the method inventions covered by the patents, and to sell the boxes in the United States."

Appellant contends, and it is not disputed, that under the license agreement licensee has paid all ad valorem taxes due on the machines.

The Supreme Court of Mississippi held that:

"In other words, the statute defined 'doing business', the corporation operated within that definition, and it was liable for the tax. * * * The terms of the contract can be enforced under the laws of this State. A violation thereof can make the lessee amenable to the process of the state courts. Hence the tax is imposed in return for protection by the state."

Therefore, the Supreme Court of Mississippi held that appellant must pay a privilege tax for the privilege of

owning patented machines and patents for the manufacture of boxes, which patents are made the subject of a license agreement in its office in New Jersey. Undoubtedly, appellant is engaging in Mississippi in interstate commerce, and an undomesticated foreign corporation has the right to engage in Mississippi in interstate commerce without obtaining a license or without paying for the privilege, as this privilege flows from the commerce clause of the Federal Constitution. *Spector Motor Service, Inc. v. O'Connor,* 71 S. Ct. 508, 95 L. ed. 573, 340 US 609-10; *Memphis Steam Laundry v. Stone,* 96 L. ed. 436 72 S. Ct. 424; *Michigan-Wisconsin Pipe Line Company v. Calvert,* 74 S. Ct. 396; *Trunkline Gas Co. v. Coleman, Advance Sheets,* 98 L. ed. 42, Case No. 179.

(A) Contrary to the opinion expressed by Appellee, State Tax Commission, the doctrine of mobilia sequuntur personam is well founded in law and logic. The Courts have always adhered to the principle as stated in *Kelly v. Bastedo,* 220 Pac. 2d 269, in which this Court has always concurred that "situs in cases of intangibles now signifies jurisdiction over them rather than its old connotation of location."

In order to constitute a business situs where intangible property may be taxed other than the owner's domicile, it must be shown that possession and control of the property has been localized in some independent business or investment activity away from the owner's domicile so that its substantial use and value primarily attach to and become an asset of the outside business. This Court has said in *McCulloch v. Maryland,* 17 US 316, 4 L. ed. 579:

• • •

"The sovereignty of a state extends to everything which exists by its own authority, or is introduced by

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its permission; but does it extend to those means which are employed by Congress to carry into execution — powers conferred on that body by the people of the United States? We think it demonstrable that it does not. Those powers are not given by the people of a single state. They are given by the people of the United States, to a government whose laws, made in pursuance of the constitution, are declared to be supreme. Consequently, the people of a single state cannot confer a sovereignty which will extend over them.

"If we measure the power of taxation residing in a state, by the extent of sovereignty which the people of a single state possess, and can confer on its government, we have an intelligible standard, applicable to every case to which the power may be applied. We have a principle which leaves the power of taxing the people and property of a state unimpaired; which leaves to a state the command of all its resources, and which places beyond its reach, all those powers which are conferred by the people of the United States on the government of the Union, and all those means which are given for the purpose of carrying those powers into execution. We have a principle which is safe for the states, and safe for the Union. We are relieved, as we ought to be, from clashing sovereignty; from interfering powers; from a repugnancy between a right in one government to pull down what there is an acknowledged right in another to build up; from the incompatibility of a right in one government to destroy what there is a right in another to preserve. We are not driven to the perplexing inquiry, so unfit for the judicial department, what degree of taxation is the legitimate use, and what degree may amount to the abuse of the power. * * * "

In *Curry v. McCanless*, 307 US 357, to which Appellee refers, it can readily be determined that the intangible assets were located within the State for the purpose of investment and reinvestment and had been localized so as to confer jurisdiction by the State.

(B) Contrary to the opinion expressed by Appellee, the Appellant *did* raise a substantial Federal question in its declaration filed in the State Court so as to bring the matter before the Supreme Court of the State of Mississippi (R 3), and which Court recognized that these matters were squarely before it by the following statement:

> "The appellant contends that the tax here collected was two per cent of the gross income of appellee from its business of renting or leasing tangible personal property in the State. On the contrary, the appellee contends that the income in question did not arise from rents, but was royalty, and, as such, was not taxable. The decision of this controversy also involves a consideration of what constitutes doing business, the situs of property for taxation, and the commerce clause of the federal constitution."

While this Court has continuously held that interstate commerce may be made to pay its way, it has also continuously held that no state may impose a privilege tax or license against the interstate transactions between the states.

In *Crutcher v. Kentucky*, 141 U. S. 47, 57, this Court said:

> "To carry on interstate commerce is not a franchise or a privilege granted by the State; it is a right which every citizen of the United States is entitled to exercise under the Constitution and laws of the United States;

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and the accession of mere corporate facilities, as a matter of convenience in carrying on their business, cannot have the effect of depriving them of such right, unless Congress should see fit to interpose some contrary regulation on the subject. * * * We have repeatedly decided that a state law is unconstitutional and void which requires a party to take out a license for carrying on interstate commerce, no matter how specious the pretext may be for imposing it."

In the case of *Freeman v. Hewit*, 329 U. S. 249, cited by Appellee, the Court actually stated:

"A State is also precluded from taking any action which may fairly be deemed to have the effect of impeding the free flow of trade between states. It is immaterial that local commerce is subjected to a similar encumbrance. It may commend itself to a State to encourage a pastoral instead of an industrial society. That is its concern and its privilege. But to compare a State's treatment of its local trade with the exertion of its authority against commerce in the national domain is to compare incomparables. * * *

"It has been suggested that such a tax is valid when a similar tax is placed on local trade, and a specious appearance of fairness is sought to be imparted by the argument that interstate commerce should not be favored at the expense of local trade. So to argue is to disregard the life of the Commerce Clause. Of course a State is not required to give active advantage to interstate trade. *But it cannot aim to control that trade even though it desires to control its own.* It cannot justify what amounts to a levy upon the very process of commerce across State lines by pointing to a similar hobble on its local trade. It is true that the existence of a tax on its local commerce detracts from the deter-

rent effect of a tax on interstate commerce to the extent that it removes the temptation to sell the goods locally. But the fact of such a tax, in any event, puts impediments upon the currents of commerce across the State line, while the aim of the Commerce Clause was precisely to prevent States from exacting toll from those engaged in national commerce. • • •

"Nor is there any warrant in the constitutional principles heretofore applied by this Court to support the notion that a State may be allowed one single taxworth of direct interference with the free flow of commerce. An exaction by a State from interstate commerce falls not because of a proven increase in the cost of the product. What makes the tax invalid is the fact that there is interference by a State with the freedom of interstate commerce."

And in the more recent cases this Court has refused to sanction such a tax in *Trunkline Gas Company v. Coleman, Advance Sheets,* 98 L. ed. 42, Case No. 179; *Michigan-Wisconsin Pipeline Co. v. Calvert,* 74 S. Ct. 396; *Memphis Steam Laundry v. Stone,* 96 L. ed 436; and *Spector Motor Service v. O'Connor,* 95 L. ed. 573.

## III

## THE OPERATING INCIDENCE OF THIS TAX IS UPON INTERSTATE COMMERCE, AS SUCH, AND NOT UPON ACTIVITIES WHICH HAVE BECOME LOCALIZED WITHIN THE BORDERS OF THE STATE.

Appellant is not present in Mississippi for any purpose, and, therefore, there is no local activity to which such a tax may attach. The Appellant is not engaged in the manufacture of either machines or boxes for sale and is not renting or leasing tangible personal property,

as its only activity is the licensing of patented rights, all of which license agreements are executed in New Jersey, where the contract is made, where the patented machine is delivered and where the royalty is received.

In all cases cited by Appellee, International Harvester Company v. Wisconsin, 322 US 435; New York v. Graves, 299 US 366; and Curry v. McCanless, 307 US 357, the taxpayer was present in each instance with his property, holding himself out to be doing business within the borders of that State, whereas, in the instant case the Appellant does not enter the State of Mississippi for any purpose.

The record will show that ad valorem taxes are paid on the machines by the licensee, which is in accordance with the agreement of license, and that all taxes are paid to the State of New Jersey required by that State, and which include an accounting for all royalty received from the State of Mississippi.

Appellee contends that even though Appellant's entire activities were solely in interstate commerce this Court is bound by the construction of a State taxing statute as announced by the highest court of the state, ignoring the principle that the taxing statute is violative of the Commerce Clause of the Constitution of the United States.

This Court has answered the above in *McLeod v. J. E. Dilworth et al*, Decided May 15, 1944, 322 U. S. 327. The Court stated:

> "A foreign corporation not qualified to do business in Arkansas, having its home office and place of business without the state, solicits orders in Arkansas by mail, telephone, or by traveling representatives. The orders are accepted at the home office and the goods delivered to carriers at this point for shipment to pur-

chasers in Arkansas. Neither the former sales nor the present gross receipts tax levied by Arkansas can be imposed upon such shipments, because the sale — the transfer of ownership — was made without the state in each instance. For Arkansas to impose a tax on such sales would be to project its powers beyond its boundaries and to tax an interstate transaction."

WHEREFORE, Appellant respectfully moves that the motion filed by the Appellee opposing jurisdiction and requesting this Court to dismiss Appellant's appeal or affirm the judgment of the Supreme Court of Mississippi be dismissed and that the appeal of Stapling Machines Co., Appellant in this cause, be considered on the record and the jurisdictional compliance.

Respectfully,

STAPLING MACHINES CO.

By .....

Of Counsel for Appellant

CERTIFICATE

I, B. L. Tighe, Jr., Counsel for Appellant in the above styled cause, certify that I have this day delivered a copy of the above and foregoing Brief of Appellant in Reply to Statement of Appellee Opposing Jurisdiction and Motion to Dismiss or Affirm, to Honorable John E. Stone, attorney for Appellee, by leaving a copy thereof at his offices located in the State Office Building, Jackson, Mississippi. This the 10th day of June, 1954.

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